IN THE

Supreme Court of the United States

OCTOBER TERM, 1945

ARMOUR AND COMPANY, an Illinois Corporation,
Petitioner,

vs.

CHESTER BOWLES, Price Administrator,
Respondent

BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES EMERGENCY COURT OF APPEALS

Preliminary Statement

We refer to the foregoing petition for a citation of the opinion below, statement of grounds of jurisdiction, citation of the statute involved, and a summary statement of the case.

It seems necessary to emphasize here only the fact that this case involves a pioneer construction of the Emergency Price Control Act of 1942; that the interpretation placed by the Price Administrator and by the court on the statutory requirements for fixing maximum prices has far-reaching consequences, not only to the producers of meat and the

processors of the many by-products of animal slaughter, but to the producers and consumers of a host of other essential commodities supplied by multi-product industries.

Specification of Errors

The following are urged as the errors of the United States Emergency Court of Appeals:

1. The court erred in not holding Revised Maximum Price Regulation 169 invalid as being arbitrary and capricious, not in accordance with law, and a violation of petitioner's rights under the Fifth Amendment of the Constitution;

2. The court erred in holding that the prices established by Revised Maximum Price Regulation 169 are "generally fair and equitable" as required by Section 2(a) of the Emergency Price Control Act of 1942, as amended;

3. The court erred in holding that the prices established by Revised Maximum Price Regulation 169 allow "a generally fair and equitable margin for * * * processing" as required by Section 3 of the Stabilization Act of 1942;

4. The court erred in holding that the so-called McKellar amendment in Section 3 of the Stabilization Act of 1942 (which provided "* * * that in the fixing of maximum prices on products resulting from the processing of agricultural commodities, including livestock, a generally fair and equitable margin shall be allowed for such processing * * *") "did not modify the basic statutory standard in Section 2(a) that maximum prices must be 'generally fair and equitable'; which would naturally mean that the prices established must allow a generally fair and equitable margin";

5. The court erred in rejecting the "cut-out" Test Method of beef cost accounting;

6. The court erred in holding that where "* * * industry earnings are above their normal peacetime

level, no adjustment of maximum prices is required if, at established ceilings, the cattle operations are producing enough to cover out-of-pocket costs in respect thereto";

7. The court erred in treating all products containing any material derived from the slaughter of cattle as a single product;

8. The court erred in defining "out-of-pocket costs" so as to exclude general overhead, such as administrative and selling expenses.

9. The court erred in sustaining a discrimination as to prices between producers of the same commodity by including subsidies as an economic factor in price regulation and approving differential subsidies, not based on different cost of production, but based solely on the fact that some producers make profits out of the production of other commodities which the Price Administrator charges off against losses through the production of under-priced commodities.

ARGUMENT

I

Revised Maximum Price Regulation 169 is invalid because it requires the sale of carcass beef and wholesale cuts at prices which do not return the cost of production.

The Emergency Price Control Act of 1942 (Sec. 2(a)) authorized the Price Administrator to establish maximum prices for commodities which would be "generally fair and equitable." Certain standards were provided to guide the administrative judgment, but the dominant rule was laid down in the broad phrase "generally fair and equitable."

As the court found, the Administrator acted upon the theory that "even without ceiling prices on live cattle, the influence of wholesale beef ceiling prices would result in maintaining the historical relationships between wholesale

beef and livestock prices." As the court further held, "Unfortunately, this theory did not seem to work out under the abnormal conditions of a wartime economy. Soon after RMPR 169 was issued, cattle prices began to rise; the cattle prices on which the regulation appears to have been predicated were soon left behind in the rising market" (R. 444).

The inevitable result of the failure of the Administrator's theory was that slaughterers of cattle were compelled to sell beef at prices which, because of the price of livestock, did not return to the slaughterers their costs of production. In the language of the Economic Adviser to the Administrator, quoted by the court, the processors "got a miserable shellacking for 9 months, an inexcusable shellacking" (R. 445).

In order to improve this situation, a program was adopted of paying subsidies to the slaughterers and (again quoting the court), "The Administrator relies heavily upon the operation of the subsidy program as sustaining the present validity of RMPR No. 169" (R. 447). Therefore, the subsidy payments must be regarded essentially as additions to the maximum prices. The question thus presented is whether the maximum price fixed for beef, plus the subsidy payment, covers the cost of production of such beef.

It is important here to note that non-processing slaughterers (those who slaughtered cattle and sold the beef and the raw by-products, but did not process the by-products) were granted a special additional subsidy of 80 cents per cwt. beyond the subsidy granted to processing slaughterers. Therefore the Administrator must concede that, since the actual costs of slaughtering beef and selling the by-products do not differ materially between processing and non-processing slaughterers, the former must lose 80 cents per cwt. more than the latter. Yet on the very day when the court held that beef prices were "generally fair and equitable" for the processing slaughterers, the same court held that the same

prices were inadequate and invalid for non-processing slaughterers.[5]

We will discuss later in this brief the legality of this discrimination between producers of the same commodity. We refer to it now in order to emphasize the point that on the record there is no question that maximum prices for beef are insufficient to reimburse the slaughterer of beef for the cost of cattle and the total cost of slaughtering and dressing, minus the revenue obtained by *selling* the by-products.

It was the Administrator's original and favorite contention that if all the profits derived from all of Armour's varied operations equalled or exceeded peacetime earnings, the maximum prices fixed for beef should be sustained regardless of any showing as to the costs of beef production. The court rejected this contention, in the following language:

> "He falls back, therefore, on the primary test of over-all profits, which indiscriminately includes not only the profits of the industry attributed to cattle operations but also an important part of the industry's profits not in any way attributable to the domestic slaughter of cattle. But if this over-all profits test were to be sustained, it would tend to produce the result mentioned in the italicized portion of the memorandum quoted in the *Gillespie* case and set forth above. It would be saying in substance that the Administrator has power to subsidize the consumer in his purchases of beef to the extent that the present over-all profits of the industry are above those of the base period. There would be no legal limitation to the extent to which the Administrator could depress prices of a given commodity so long as

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[5] Shortly after this decision, the court entered an order, April 2, 1945, setting aside the judgment in favor of non-processing slaughterers, in conformity with an agreement between these slaughterers and the Price Administrator whereby the reduction of the 80-cent special subsidy to 30 cents, which had been ordered to take effect April 1st, would be abandoned and the full 80-cent special subsidy continued for the benefit of non-processing slaughterers. (*Heinz et al.* v. *Bowles, supra,* p. 8.)

the industry as a whole maintained its base period earnings."

In support of this rejection of the over-all profits test, we should point out the evidence, not contradicted, that certain Armour operations (oil products, oil mills, canned foods other than meat, poultry and dairy, sandpaper, ammonia, storage, trucking, Havana fertilizers, spice, chemicals, fertilizers, foreign operations, car lines, and miscellaneous) showed a combined profit in 1943, not attributable to any domestic slaughter, amounting to $19,901,000 (R. 118). Additional profits of processing departments, attributable solely to pork, sheep, and calf slaughter and not to cattle slaughter, amounted in 1943 to $15,029,000.

The total profits of these operations, amounting to $34,930,000, should be considered in connection with the reference in the opinion of the court to Armour's profits, *before taxes*, amounting to $36,000,000. This makes it clear that the Administrator was insisting, in effect, that Armour should be compelled to sell beef at a loss (although non-processing slaughterers could not be so compelled), not because Armour was making money indirectly out of cattle slaughter, but because Armour was making enough money out of other industrial operations so that it could meet beef losses and still continue in business. This meant that while the government found it necessary to "subsidize the consumer in his purchases of beef" from non-processing slaughterers, the government was seeking to compel Armour to subsidize the consumer in his purchases of beef produced by Armour.

The court has, however, modified the Administrator's insupportable theory of over-all profits and approved the theory that since a few large slaughterers, such as the present petitioner, process their by-products instead of selling them to separate processors, there should be deducted from

the cost of beef, not merely the market value of the raw by-products, but all the *profits* made by the subsequent processing of the by-products. Here is a simple example:

One by-product of cattle slaughter is hides. The great majority of slaughterers sell hides—for which there are ceiling prices fixed by OPA. The present petitioner and a very few other packers sell hides, in part to outsiders and in part to the Leather Division of the company's operations. This Leather Division also buys hides in the general market. So the Leather Division operates as a separate business, the cost of its raw materials being largely the price paid for hides, which is the ceiling price. The Leather Division sells its leather, for which there are also ceiling prices. The leather industry is a separate industry in which the petitioner is in competition with many large producers who are not slaughterers.

In a similar manner, the petitioner makes soap, buying its raw materials, oils, etc. (at ceiling prices) and selling its products (at ceiling prices) in competition with such large independent concerns as Procter & Gamble, Colgate-Peet-Palmolive, and Lever Brothers.

Only a limited number of slaughterers engage in these various industries, which process raw materials which are in part by-products of cattle slaughter. Thus maximum prices for beef are sustained for one "industry" on the basis of the profits of the operations of several *other* industries in which a *few* of the meat-packers engage. These few do represent a large volume of the slaughtering business, but they are only a small fraction of the numbers engaged. Hence a special subsidy has been found necessary to save a large number of enterprises from insupportable losses.

It is now the modified contention of the Administrator, sustained by the court, that all the profits of processing by-

products of cattle slaughter should be credited against the cost of beef, and thereby losses on beef should be eliminated which would be inevitable if only the revenue from the *sale* of raw by-products were credited against the cost of producing beef.

The petitioner contends that the cost of producing beef should be determined for Armour, as well as for non-processing slaughterers, by the established cut-out Test Method of accounting. Against this contention, the court has held that all profits from the processing of by-products of cattle slaughter (which can be attributed to the use of such by-products) should be credited to the Beef Division and, if then the Beef Division as a whole has recovered its "out-of-pocket costs," the maximum prices for a single commodity, such as beef, will be sustained.

The result of this holding is to approve maximum prices for a commodity which deny *some* producers the cost of production of that commodity, while at the same time *increased* maximum prices are authorized for *other* producers of the same commodity through the device of a subsidy. This inequity and discrimination in price-fixing is supported by the adoption of novel methods of accounting for part of an industry, despite the express provisions of the Emergency Price Control Act. Thus, the first legal question presented is whether the Administrator, under the statute, had authority to disregard established accounting methods and practices in determining cost of production, and whether or not the court erred in rejecting and approving the Administrator's disregard of the cut-out Test Method of accounting.

II

The cut-out Test Method of determining costs of producing beef is the long-established method and practice which the Administrator had no authority to disregard.

The Emergency Price Control Act of 1942 provided, in Section 2(h), as follows:

> "The powers granted in this section shall not be used or made to operate to compel changes in the business practices, cost practices or methods, or means or aids to distribution, established in any industry, except to prevent circumvention or evasion of any regulation, order, price schedule, or requirement under this Act."

By amendment in the Stabilization Extension Act of 1944, the foregoing provision was strengthened to read as follows:

> "The powers granted in this section shall not be used or made to operate to compel changes in the business practices, cost practices or methods, or means or aids to distribution, established in any industry, or changes in established rental practices, except *where such action is affirmatively found by the Administrator to be necessary* to prevent circumvention or evasion of any regulation, order, price schedule, or requirement under this Act." (Amendment italicized)

Also in the Stabilization Extension Act of 1944, Section 2(a) of the Emergency Price Control Act (which authorized and set the standards for price-fixing) was amended to include the following proviso referring to any price-fixing regulation or order:

> "*Provided*, That no such regulation or order shall contain any provision requiring the determination of costs otherwise than in accordance with established accounting methods."

The purpose and intent of the foregoing provisions should be obvious. The history of the Emergency Price Control Act showed a determined intention on the part of Congress to deny any power to the Administrator to compel changes in established business practices or cost accounting methods. The Administrator might try to compel such changes by ordering the adoption of novel practices or accounting methods. Any such order would be plainly forbidden by the foregoing language of the Act.

But the Administrator is here found seeking to accomplish all the evil of an order to compel changes, by requiring businessmen to do things which could only be done by a change of business practice and by requiring businessmen to set up statistics in such a manner as will permit the Administrator to adopt novel accounting methods and to arrive at novel accounting results.

Certainly that which the Congress forbade the Administrator to do directly, the Congress did not intend to authorize the Administrator to do indirectly. Yet, when the Administrator fixes prices by utilizing a novel accounting method of determining cost of production, he is certainly requiring a businessman to determine his costs "otherwise than in accordance with established accounting methods."

It is startling to read the Emergency Court's interpretation of the statutory requirement. The opinion of the court reads:

> "* * * RMPR 169 contains no provision *requiring* changes in cost accounting methods; the industry remains free to follow its old cost accounting practices. The Administrator has merely refused to accept the cut-out test method used in the industry as the yardstick for determining whether the maximum prices are generally fair and equitable. It surely was not the intention of Congress to require the Administrator, in discharging his duties under Sec. 2(a), to accept at face value the results indicated by whatever method of cost

> accounting the industry has chosen to pursue. For the same reason, we hold that the regulation does not operate 'to compel changes in the business practices, cost practices, or methods * * * established in any industry,' contrary to the prohibition of Sec. 2(h) of the Act as amended." (Italics by the court) (R. 459)

We submit that this interpretation of the statute offers a shocking encouragement to an executive official to evade the plain statutory mandate from which alone his authority proceeds. As an exercise in dialectics, it may be possible to assert with a straight face that the meat-packing industry is not *required* to change its cost accounting methods; that it "remains free to follow its old cost accounting practices." But the prices for its products are being fixed by entirely different accounting methods so that the freedom of the industry to follow its old cost accounting practices is like the freedom of a man who is not *required* to walk to jail, but who will be given a ride by the police!

The court further holds that:

> "* * * the McKellar Amendment [6] did not modify the basic statutory standard in Section 2(a) that maximum prices must be 'generally fair and equitable', which would naturally mean that the prices established must allow a generally fair and equitable margin."

Obviously, the purpose of an amendment to a law is either to change the law or to change or prevent a misinterpretation of the law. But the court supports its effort to make this amendment meaningless by quoting from a statement in the Senate by the Senator in charge of the bill explaining that the "Amendment is *in line* with the policy already established by the *Price Control Act*, and I believe it is *substantially* a restatement of existing law." (Italics ours).

There would have been no need for the amendment if the Price Administrator had previously interpreted the words

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[6] The McKellar Amendment is printed in Appendix, *infra*, p. 38.

"generally fair and equitable" prices so as to provide that "a generally fair and equitable margin shall be allowed for such processing" (of agricultural commodities, *including livestock*). The amendment may have been "substantially a restatement of existing law" as the Congress *intended* the law to be interpreted. It may have been "in line with the policy already established by the Price Control *Act*." It was necessary, however, because the policy established by the Price *Administrator* was denying a fair and equitable margin for the processing of agricultural commodities. The court has completely misinterpreted the meaning of the senatorial statement quoted. The purpose of the amendment was to compel the Price Administrator to change his policy. That is what he has not done and yet the court sustains him in continuing to disregard the mandate of the law. If the established cut-out Test Method of accounting had been followed, then it would have been made crystal clear that the Administrator was not allowing a fair and equitable margin for processing cattle.

There is no doubt that the cut-out Test Method is the long-established method of determining the cost of beef. A brief explanation is found in the note as page 5, *supra*. According to an authoritative writer quoted by the court, "This is the accepted method of computing the cost of a dressed carcass; and it is the method that the packer must follow if he is to conduct his business intelligently" (R. 451).

The Administrator has contended that losses determined by the cut-out Test Method are mere "bookkeeping losses." This contention is based on an assumption contrary to fact—an assumption that there is a difference between the selling price of raw by-products, when they are sold by non-processing slaughterers, and the selling price of the same by-products when they are transferred by a processing slaughterer to a processing division. In a word, it will be conceded

that when a non-processing slaughterer sells a hide, he obtains for it only the ceiling price. Therefore, he can only credit that ceiling price against his cost of producing beef. But it is apparently assumed by the Price Administrator that, when Armour's Beef Division sells a hide to Armour's Leather Division, at the same ceiling price, then the cost charged to the Leather Division could be increased or decreased, and therefore that the credit to the Beef Division could be increased or decreased. But the Leather Division could not operate as a sound business in such a manner.

The Leather Division buys hides normally at ceiling prices and, whether they are bought from Armour's Beef Division or from outsiders, they must be charged in normally at ceiling prices. Therefore, no other credit could be given to the Beef Division except the same credit as though hides had been sold to a stranger. Since there have always been market prices and there are now ceiling prices for all the by-products of cattle slaughter, it is perfectly clear that the costs of producing carcass beef are exactly those determined by the cut-out Test Method.

On the other hand, the contention that the profits of processing by-products should be credited against the costs of beef production is simply the contention that the profits of several industries shall be credited to one industry in order to justify prices which compel that single industry to operate at a loss.

The theory approved by the court is, however, that in an integrated industry some commodities may be sold at a loss because their production is justified, not by their immediate profits, but by profits to be derived from by-products. It was the effort of the Administrator to prove that this was historically true as to beef, in the packing industry. But this effort failed because, although limited losses on beef production might be found intermittently in the case of a

few large integrated packers, it was obvious, first, that no such losses as now imposed had ever been suffered, and, second, that the major number of slaughterers had to seek their profits out of the sale of beef and the sale of raw by-products, and could not count on the profits of processing operations to offset losses in the sale of beef.

We submit, therefore, at the outset, that the Administrator's disregard of the cut-out Test Method of accounting was in violation of the specific requirements of the Act both as to following established accounting methods and as to fixing generally fair and equitable prices. But since the court likewise rejected the cut-out Test Method and allocated proportionate profits of by-product operations as credits to the cost of producing beef, we must analyze the basis for the judgment of the court.

III

Even allocating the profits of by-product operations as a credit against the cost of producing beef, the maximum prices for beef did not return cost of production.

The theory of the Administrator that, since the total profits of Armour and Company operations were above peacetime earnings, Armour and Company could not complain of prices that did not return the cost of production of beef, was rejected by the court. It obviously had no support in the law which authorized the Price Administrator, not to regulate industrial profits, but to fix the prices of separate commodities.

But the court took the position that in a multi-product industry, if the industry maintained aggregate peacetime earnings, it would be sufficient to validate the maximum price of a particular commodity if that maximum price covered the "out-of-pocket costs" of that commodity. The

court took the further position that the prices fixed for beef would be "generally fair and equitable" "and would allow a generally fair and equitable margin for * * * processing" if "cattle operations as an entirety" (which would include pharmaceuticals, soap, leather, etc.) were "treated as a single product or as a closely related group of products."

There is nothing in the statute which authorizes the Administrator to fix prices for "operations" producing several commodities, or to treat the combined products of the beef industry, the leather industry, the soap industry, etc. as a single industrial product. But, if we overlook the impropriety of an amendment of the statutes by the Emergency Court, and assume that in some way all cattle operations can be treated under the statute as a single industrial product, we still find that *after crediting all the profits from the by-products of cattle slaughter to the Beef Division,* the Beef Division still operates at a loss! (R. 120).

This situation compelled the court, in sustaining the Administrator, to incorporate in its opinion another novel creation of judge-made law. Without any warrant in the statute, the court announced the theory that, if an industry maintained peacetime earnings, and if the current maximum price of a particular product covered the "out-of-pocket costs" of producing that commodity, then such a maximum price could be held valid, even though it failed to cover *all* costs of production.

It was made plain by the court that "out-of-pocket costs" did *not* cover *all* costs of production. The court did not undertake to define precisely what it meant by "out-of-pocket costs," which is unfortunate since it may be difficult for anyone else to determine how the court thinks the phrase should be defined. But the court did say that out-of-pocket costs "included direct labor and material costs and undoubtedly *excluded* general overhead such as administrative and selling expenses" (R. 457).

There cannot be the slightest question that overhead, administrative and selling expenses are parts of a cost of production. They are "out-of-pocket costs" in the sense that they have to be paid for. It may be possible to argue that a return on investment need not be included in the definition of "out-of-pocket costs." It should be suggested, however, that it is just as necessary for a business to make a return on its investment as it is to pay for labor and materials if the business is to continue in operation. If a business occupies a leased building, it must pay rent in order to continue, and, by the same token, prices fixed by the government should be sufficient to pay interest to bondholders and a return to stockholders on their investment.

But it is arguable that, if an industry generally and the enterprises therein are making normal earnings, the maximum price of a particular commodity may be sustained if it covers only the "out-of-pocket costs" of producing that commodity. However, it is difficult to understand how administrative and selling expense is any less a "cost" that must be repaid in the selling price than labor and material cost. Labor and material are useless without administrative direction. Products do not move themselves either physically, which requires the payment of packing and transportation expense, or commercially, which requires the payment of selling expenses. All the administrative and selling expenses blithely ignored by the court are actual out-of-pocket payments which are attributable, and allocated, to beef production, and allowed by the Bureau of Internal Revenue as deductible expenses in arriving at net income. Sixty percent represents salaries paid to employees who are just as essential to beef production as the workers to whom wages are paid for slaughtering and dressing beef. The other forty percent represents such expenses as packing, delivering, transportation, heat, light, power, taxes, and rent, without which payments the business of beef production could not continue. (Exhibit XI, R. 125)

Yet the court could find no ground for sustaining the maximum prices fixed for beef and dismissing the complaint except by proceeding, step by step, as follows: First, reject (for Armour) the established accounting method of determining the cost of producing beef; second, credit to beef production proportionately all the profits of by-product operations related to cattle slaughter; third, treat cattle operations as an entirety with a single product; fourth, allow only "out-of-pocket costs" in cost of production; fifth, define "out-of-pocket costs" so as to eliminate from the allowance several million dollars of actual out-of-pocket payments.

We submit that, step by step, the Administrator, with the supporting arm of the court, has moved away from statutory requirements, has undertaken to exercise an authority not granted, but specifically denied, has fixed prices for a commodity which, under no possible definition, can be defined as "generally fair and equitable," or as allowing "a generally fair and equitable margin * * * for processing." Complaint against these same prices by non-processing slaughterers, based on the cut-out Test Method of figuring cost of production, has been recognized by the government as just, in the grant of an additional 80-cent subsidy to such slaughterers, and even then further sustained by the same court which rejected the petitioner's complaint.

There is only one valid distinction to be drawn between the two inconsistent rulings; there is only one real basis for the denial of petitioner's complaint, and that is the wholly illegal basis that petitioner is making more money out of all its varied industrial operations, including a mass of operations in no way related to cattle slaughter, than it made in peacetime. But we submit that taxation and the recapture of profits is the function of the Congress and the Treasury; and this duty has not been delegated, nor could it be constitutionally delegated, to the Price Administrator.

Furthermore, we submit that it is utterly unjust to the

industry as a whole to utilize the profits made by one enterprise largely out of other industrial operations, as the means of denying to the industry as a whole a fair maximum price for *its* products.

This petition presents, not a plea for sympathy or for aid to the downtrodden and the oppressed, but a simple plea for the establishment and maintenance of a rule of law and equal justice. We submit that there is no legal justification for the enforcement by the Administrator of maximum prices for beef which concededly fall far short of covering actual cost of production. We submit that the Emergency Court has found no reasons for sustaining such prices and for dismissing the complaint which can be accepted as legal reasons.

We submit that the extension of the legal theory required to support the Price Administrator in the present case would permit him to exercise an arbitrary and dictatorial control over, not only this industry, but over every multi-product industry in the United States, which was not intended, but, in fact, is expressly forbidden in the law creating his authority.

We submit that maintaining the integrity of the law as enacted by the Congress, and preserving the constitutional rights of petitioner and others subjected to the control of administrative orders not authorized by or in accordance with the law, is a matter of grave public importance, and worthy of serious and exhaustive consideration by this honorable Court.

Dated: April 28, 1945.

Respectfully submitted,

DONALD R. RICHBERG,
CHARLES J. FAULKNER,
FREDERICK R. BAIRD,
GEORGE E. LEONARD, JR.,
Attorneys for Petitioner.